

# **SAN BENITO COUNTY**

Audit Report

## **APPORTIONMENT AND ALLOCATION OF PROPERTY TAX REVENUES**

*July 1, 2015, through June 30, 2020*



**BETTY T. YEE**  
California State Controller

January 2022



**BETTY T. YEE**  
California State Controller

January 5, 2022

The Honorable Joe Paul Gonzalez, Auditor-Controller  
San Benito County  
440 Fifth Street, Room 206  
Hollister, CA 95023

Dear Mr. Gonzalez:

The State Controller's Office audited San Benito County's process for apportioning and allocating property tax revenues to determine whether the county complied with California statutes for the period of July 1, 2015, through June 30, 2020. We conducted the audit pursuant to the requirements of Government Code section 12468.

Our audit found that the county incorrectly calculated the:

- Jurisdictional changes;
- Negative Educational Revenue Augmentation Fund adjustments; and
- Vehicle License Fee adjustments.

If you have any questions, please contact Lisa Kurokawa, Chief, Compliance Audits Bureau, by telephone at (916) 327-3138.

Sincerely,

*Original signed by*

KIMBERLY TARVIN, CPA  
Chief, Division of Audits

KT/as

cc: Leann Godinez, Assistant Auditor-Controller  
San Benito County  
Kelsey MacIsaac, Auditor-Accountant II  
San Benito County  
Bea Gonzales, Chair  
San Benito County Board of Supervisors  
Chris Hill, Principal Program Budget Analyst  
Local Government Unit  
California Department of Finance

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# Audit Report

## Summary

The State Controller's Office (SCO) audited San Benito County's process for apportioning and allocating property tax revenues to determine whether the county complied with California statutes for the period of July 1, 2015, through June 30, 2020.

Our audit found that the county incorrectly calculated the:

- Jurisdictional changes;
- Negative Educational Revenue Augmentation Fund (ERAF) adjustments; and
- Vehicle License Fee (VLF) adjustments.

## Background

After the passage of Proposition 13 in 1978, the California State Legislature (Legislature) enacted new methods for apportioning and allocating property tax revenues to local government agencies, school districts, and community college districts. The main objective was to provide these agencies and districts with a property tax base that would grow as assessed property values increased. The method has been further refined in subsequent laws passed by the Legislature.

One key law was Assembly Bill 8, Chapter 282, Statutes of 1979, which established the method of allocating property taxes for fiscal year (FY) 1979-80 and subsequent fiscal years. The methodology is commonly referred to as the "AB 8 process."

Property tax revenues are apportioned and allocated to local government agencies, school districts, and community college districts using prescribed formulas and methods defined in the Revenue and Taxation Code. In general, the amount of revenue an agency or district receives is based on the amount received in the prior year plus a share of the property tax growth within its boundaries.

The AB 8 process involves several steps, including the transfer of revenues from school and community college districts to local government agencies and the development of the tax rate area (TRA) annual tax increment (ATI) apportionment factors, which determine the amount of property tax revenues to be allocated to each jurisdiction.

The total amount to be allocated to each jurisdiction is then divided by the total amount to be allocated to all entities to determine the AB 8 factor (percentage share) for each entity for the year. The AB 8 factors are computed each year for all entities using the revenue amounts established in the prior year. These amounts are adjusted for growth annually using ATI apportionment factors.

Subsequent legislation removed from the AB 8 process revenues generated by unitary and operating nonunitary properties, pipelines, regulated railway companies, and qualified electric properties. These revenues are now apportioned and allocated under separate processes.

Other legislation established an ERAF in each county. Most local government agencies are required to transfer a portion of their property tax revenues to the fund. The fund is subsequently apportioned and allocated to school and community college districts by the county auditor according to instructions received from the county superintendent of schools or the chancellor of the California community colleges.

Revenues generated by the different types of property tax are apportioned and allocated to local government agencies, school districts, and community college districts using prescribed formulas and methods, as defined in the Revenue and Taxation Code. Taxable property includes land, improvements, and other properties that are accounted for on the property tax rolls, which are primarily maintained by the county assessor. Tax rolls contain an entry for each parcel of land, including parcel number, owner's name, and value. The types of property tax rolls are:

- *Secured Roll*—Property that, in the opinion of the assessor, has sufficient value to guarantee payment of the tax levies and that, if the taxes are unpaid, the obligation can be satisfied by the sale of the property by the tax collector.
- *Unsecured Roll*—Property that, in the opinion of the assessor, does not have sufficient permanence or other intrinsic qualities to guarantee payment of taxes levied against it.
- *State-Assessed Roll*—Utility properties composed of unitary and operating nonunitary value assessed by the California State Board of Equalization (BOE).
- *Supplemental Roll*—Property that has been reassessed due to a change in ownership or the completion of new construction, where the resulting change in assessed value is not reflected in other tax rolls.

To mitigate problems associated with the apportionment and allocation of property tax revenues, Senate Bill 418, which requires the State Controller to audit the counties' apportionment and allocation methods and report the results to the Legislature, was enacted in 1985.

Apportionment and allocation of property tax revenues can result in revenues to an agency or agencies being overstated, understated, or misstated. Misstated revenues occur when at least one taxing agency receives more revenue than it was entitled to, while at least one taxing agency receives less revenue than it was entitled to.

The agency that received less tax revenue than its statutory entitlement would have standing to require that adjustments be made by the county, either on a retroactive or prospective basis. SCO does not have enforcement authority or standing to require the county to take corrective action with respect to misallocation of tax revenues, unless the misallocation resulted in overpaid state funds (e.g., funds intended for the ERAF, school districts, or community college districts). SCO has authority to recover misallocations resulting in overpaid state funds pursuant to Government Code (GC) sections 12410, 12418, and 12419.5.

GC section 12410 provides the State Controller with broad authority to “superintend the fiscal concerns of the state.” GC section 12418 provides the State Controller with the authority to “direct and superintend the collection of all money due the State, and institute suits in its name” against all debtors of the State. GC section 12419.5 provides the State Controller with the authority to offset any amounts due the State against any amounts owed to the debtor by the State.

Revenue and Taxation Code (RTC) section 96.1(b) allows a reallocation of current audit findings and unresolved prior audit findings.

RTC section 96.1(c)(3) limits a cumulative reallocation or adjustment to one percent of the total amount levied at a one-percent rate of the current year’s original secured tax roll. For reallocation to the ERAF, school districts, or community college districts, a reallocation must be completed in equal increments within the following three fiscal years, or as negotiated with the State Controller.

## **Audit Authority**

We conducted this audit under the authority of GC section 12468, which requires the SCO to audit the apportionment and allocation of property tax revenues on a one-, three-, or five-year cycle, depending on the county’s population. The audit results are reported annually to the Legislature along with any recommendations for corrective action.

## **Objective, Scope, and Methodology**

Our audit objective was to determine whether the county complied with Revenue and Taxation Code, Health and Safety Code, and Government Code requirements pertaining to the apportionment and allocation of property tax revenues.

A property tax bill contains the property tax levied at a one percent tax rate, as required by Proposition 13. A tax bill may also contain special taxes, debt service levies on voter-approved debt, fees, and assessments levied by the county or a city. The scope of our audit is concerned with the distribution of the one percent tax levy. Special taxes, debt service levies on voter-approved debt, fees, and assessments levied by the county or a city are beyond the scope of our audit and were not reviewed or audited.

The audit period was July 1, 2015, through June 30, 2020.

To achieve our objective, we performed the following procedures:

- We gained an understanding of the county’s process for apportioning and allocating property tax revenues by interviewing key personnel.
- We reviewed the county’s written procedures for apportioning and allocating property tax revenues.
- We reviewed documents supporting the transaction flow for apportioning and allocating property tax revenues.

- We judgmentally selected a non-statistical sample of five from approximately 47 taxing jurisdictions within the county for all fiscal years in the audit period.<sup>1</sup> Then, we:
  - Recomputed apportionment and allocation reports to verify computations used to develop property tax apportionment factors;
  - Tested TRA reports to verify that the correct TRA factors were used in the computation of the ATI;
  - Reviewed supplemental property tax administrative costs and fees to determine whether recovery costs associated with administering supplemental taxes were based on actual costs and did not exceed five percent of revenues collected, as prescribed in statute;
  - Verified computations used to develop supplemental property tax apportionment factors;
  - Verified unitary and operating nonunitary, unitary regulated railway, and qualified electric property computations used to develop apportionment factors;
  - Reviewed redevelopment agency reports and verified computations used to develop the project base amount and the tax increment distributed to the redevelopment agency;
  - Reviewed Redevelopment Property Tax Trust Fund deposits;
  - Reviewed property tax administration cost reports and recomputed administrative costs associated with work performed for apportioning and allocating property tax revenues to local government agencies, school districts, and community college districts;
  - Reviewed ERAF reports and verified computations used to determine the shift of property taxes from local government agencies to the ERAF and, subsequently, to school and community college districts (see Finding 2);
  - Reviewed the Sales and Use Tax letter and recomputed VLF computations used to verify the amount transferred from the ERAF to counties and cities to compensate for the diversion of these revenues (see Finding 3); and
  - Reviewed BOE's jurisdictional change filing logs and their impact on the tax apportionment and allocation system (see Finding 1).

Errors found were not projected to the intended (total) population.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our

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<sup>1</sup> The actual number of taxing jurisdictions, which include the ERAF, can vary from year to year based on jurisdictional changes. The five sampled taxing jurisdictions include a special district, a school district, a city, the county, and the ERAF. We selected only one of each type of local agency because when the apportionment and allocation for one jurisdiction is incorrect, the error affects every other taxing jurisdiction.

audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We did not audit the county's financial statements.

## **Conclusion**

Our audit found that San Benito County did not comply with California statutes for the apportionment and allocation of property tax revenues for the audit period, because it incorrectly calculated the:

- Jurisdictional changes;
- Negative ERAF adjustments; and
- VLF adjustments.

These instances of noncompliance are quantified in the schedule and described in the Findings and Recommendations section of this audit report.

## **Follow-up on Prior Audit Findings**

The county has satisfactorily resolved the findings noted in our prior audit report, for the period of July 1, 2008, through June 30, 2015, issued on May 3, 2016, as shown on the Appendix.

## **Views of Responsible Officials**

We issued a draft report on November 9, 2021. Joe Paul Gonzalez, Auditor-Controller, responded by letter dated November 18, 2021, agreeing with the audit results. The county's response is included as an attachment to this audit report.

## **Restricted Use**

This audit report is solely for the information and use of San Benito County, the Legislature, the California Department of Finance, and SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this audit report, which is a matter of public record and is available on the SCO website at [www.sco.ca.gov](http://www.sco.ca.gov).

*Original signed by*

KIMBERLY TARVIN, CPA  
Chief, Division of Audits

January 5, 2022

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**Schedule—**  
**Summary of Misallocations to the**  
**Educational Revenue Augmentation Fund**  
**July 1, 2015, through June 30, 2020**

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<u>Finding Number</u>	<u>Fiscal Years Affected</u>	<u>Amount Due to the ERAF</u>
3 – Vehicle License Fee adjustments	2019-20	<u>\$ 63,061</u>
Total		<u><u>\$ 63,061</u></u>

# Findings and Recommendations

## **FINDING 1— Jurisdictional changes**

During testing of the county’s jurisdictional change process, we found that the county incorrectly implemented jurisdictional changes for the City of San Juan Bautista for FY 2016-17, FY 2018-19, and FY 2019-20. As a result of these errors, affected taxing entities did not receive the correct share of property tax revenues. We could not quantify the monetary effect for each affected taxing entity due to the cumulative effect of the various errors affecting the computation and allocation. The error occurred because the county incorrectly implemented RTC section 99, which provides the legal requirements for jurisdictional changes.

A jurisdictional change involves a change in the organization or boundaries of a local agency or school district. Typically, these are service-area or responsibility changes between the local jurisdictions. As part of the jurisdictional change, the local agencies are required to negotiate any exchange of base-year property tax revenues and ATIs. Consequently, the local agency whose responsibility increased receives additional ATI, and negotiated agreements adjust the base property tax revenues accordingly.

### Recommendation

We recommend that the county

- Review RTC section 99 and update its procedures to ensure that changes to TRA numbers and factors are made pursuant to BOE change notices;
- Recalculate its ATI for FY 2016-17, FY 2018-19, and FY 2019-20; and
- Make monetary adjustments to affected taxing entities.

### County’s Response

The County agrees with this finding. The County will recalculate the annual tax increment for the three impacted fiscal years and will make monetary adjustments to the affected taxing entities.

## **FINDING 2— Negative Educational Revenue Augmentation Fund adjustments**

During testing of the county’s negative ERAF process, we found that in FY 2015-16 the county mistakenly removed money from a basic-aid school entity, Aromas/San Juan Unified, when redirecting ERAF revenue allocations. This mistake resulted in a misallocation of \$22,652 of ERAF revenues. The error occurred because the county incorrectly implemented RTC section 97.70(a)(1)(B), which provides the legal requirements for negative ERAF.

RTC section 97.70 provides the legal requirements for the calculation of negative ERAF adjustments:

In FY 2004-05, the auditor shall reduce the total amount of ad valorem property tax revenue that is otherwise required to be allocated to a county’s ERAF by the countywide VLF amount. When there is not enough ad valorem

property tax revenue that is otherwise required to be allocated to a county ERAF for the auditor to complete the allocation reduction, the auditor shall additionally reduce the total amount of the ad valorem property tax revenue that is otherwise required to be allocated to all school districts and community college districts in the county.

#### Recommendation

We recommend that the county:

- Review RTC section 97.70(a)(1)(B) and update its procedures to ensure that basic aid schools are properly identified and excluded when performing negative ERAF reallocations;
- Recalculate its negative ERAF reallocations for FY 2015-16 to ensure that Aromas/San Juan Unified is excluded; and
- Make monetary adjustments to schools and the ERAF.

#### County's Response

The County agrees with this finding. The County will make the corrections recommended by the SCO.

### **FINDING 3— Vehicle License Fee adjustments**

During testing of the county's VLF adjustment process, we found that the county incorrectly carried forward FY 2018-19 VLF adjustment amounts when performing FY 2019-20 VLF calculations. The mistake was due to clerical error and resulted in a net over-allocation of \$63,061 from the ERAF (Schedule). The FY 2019-20 VLF adjustment amounts for the county (\$40,326), the City of Hollister (\$6,536), and the City of San Juan Bautista (\$16,199) were overstated.

RTC sections 97.69 and 97.70 provide the legal requirements for VLF adjustments. The VLF permanently provided additional property tax revenues to cities and counties in lieu of the discretionary VLF revenues that these agencies previously received.

#### Recommendation

We recommend that the county:

- Review RTC sections 97.69 and 97.70 and update its procedures to include the correct past-year adjustment amounts to carry forward during the calendar year VLF adjustment process;
- Recalculate its VLF adjustment for FY 2019-20 and carry forward corrected amounts to subsequent VLF computations; and
- Make monetary adjustments to the county, the City of Hollister, the City of San Juan Bautista, and the ERAF.

#### County's Response

The County agrees with this finding. The County will recalculate its VLF adjustment for FY2019/2020 and carry forward corrected amounts to subsequent VLF computations and making any monetary adjustment to impacted taking entities.

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## Appendix— Summary of Prior Audit Findings

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The following table shows the implementation status of San Benito County's corrective actions related to the findings contained in the county's prior audit report dated May 3, 2016:

<b>Prior Audit Finding Number</b>	<b>Prior Audit Finding Title</b>	<b>Implementation Status</b>
1	Unitary and operating nonunitary apportionment	Fully implemented
2	Unitary railroad apportionment	Fully implemented
3	Vehicle Licensing Fee adjustments	Fully implemented

**Attachment—  
County's Response to Draft Audit Report**

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**Joe Paul Gonzalez**  
Auditor-Controller-Clerk-Recorder-Registrar  
E-Mail: [jgonzalez@cosb.us](mailto:jgonzalez@cosb.us)



**OFFICE OF THE COUNTY AUDITOR**

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Hollister, California 95023

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**COUNTY OF SAN BENITO**

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Scott W. Freesmeier  
Office of the State Controller  
901 Corporate Center Dr., Suite 200  
Monterey Park, CA 91754

November 18, 2021

Dear Mr. Freesmeier,

Please see our responses to your draft audit report on the methods employed by San Benito County to apportion and allocate property tax revenue for the period of July 1, 2015 through June 30, 2020.

Finding 1:

County Response: The County agrees with this finding. The County will recalculate the annual tax increment for the three impacted fiscal years and will make monetary adjustments to the affected taxing entities.

Finding 2:

County Response: The County agrees with this finding. The County will make the corrections recommended by the SCO.

Finding 3:

County Response: The County agrees with this finding. The County will recalculate its VLF adjustment for FY2019/2020 and carry forward corrected amounts to subsequent VLF computations and making any monetary adjustment to impacted taxing entities.

I appreciate the opportunity to respond to your draft audit report and findings. If you have any further questions or if our comments require any clarification, please call me at 831-636-4090.

Sincerely,

Joe Paul Gonzalez  
Clerk, Auditor & Recorder, Registrar of Voters

**State Controller's Office  
Division of Audits  
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Sacramento, CA 94250**

**<http://www.sco.ca.gov>**